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REPORT OF THE PROGRAMME AND BUDGET COMMITTEE: FINANCIAL REGULATIONS

Tax Equalization Fund

Report by the Director-General

Summary

In compliance with conclusion 1991/6 paragraph (f)(ii) of the Programme and Budget Committee, reports on the use of the Tax Equalization Fund with regard to credits assigned to Member States. Presents proposals for the texts of financial regulations 5.2 (e), 5.3 and 10.1 (b) and of staff regulations 6.8 (b), 6.8 (c) and 6.8 (d).

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Introduction

1. In its conclusion 1991/6 (para. (f)(ii) related to the programme and budgets, 1992-1993, the Programme and Budget Committee requested the Director-General to present to the eighth session of the Board details concerning the use of the Tax Equalization Fund especially with regard to the credits assigned to Member States, as well as to present proposals for the texts still in brackets, namely financial regulations 5.2 (e) and 5.3. The present report is submitted to the Board in compliance with the request of the Programme and Budget Committee.

I. USE OF THE TAX EQUALIZATION FUND

2. Upon entry into force of the Constitution of UNIDO in 1985, and the adoption for the first time of a programme and budgets for UNIDO as a separate organization, Member States were guided by Article 26.2 of the Constitution:

> "2. The rules and regulations governing the organization established by United Nations General Assembly Resolution 2152 (XXI) shall govern the Organization and its organs until such time as the latter may adopt new provisions."

3. The General Conference of UNIDO adopted financial and staff regulations for UNIDO only at its second session, held in November 1987. Until then the Financial and Staff Regulations and Rules of the United Nations remained applicable to UNIDO by virtue of Article 26.2 of the Constitution. Thus a Tax Equilization Fund was established under the United Nations Financial and Staff Regulations.

4. To the United Nations Fund were credited the revenues derived from amounts withheld from the salaries of staff members on account of staff assessment. These amounts were held to the credit of Member States in the proportion of the scale of assessment of contributions to the regular budget and, if not required in respect of a Member State to meet charges for tax refunds to staff members, the amounts were returned to Member States by

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deducting the amount of the credit from the assessment for the following fiscal period. The Staff Regulations of the United Nations authorized the Secretary-General to refund staff members the amount of their income taxes in respect of their United Nations income. Practically all Member States of the United Nations, except the United States of America, have accepted Section 18 (b) of the Convention on the Privileges and Immunities of the United Nations, according to which Officials (staff members) shall "be exempt from taxation on the salaries and emoluments paid to them by the United Nations". Thus, the real purpose of the Tax Equalization Fund was to equalize the final net remuneration of all staff members without regard to nationality by neutralizing the effect of the tax liability of United States nationals and permanent residents.

5. Upon the establishment of UNIDO as an organization separate from the United Nations, the Member States, taking into account that very few staff members of UNIDO were liable to pay income taxes on their official salaries and emoluments, initiated the practice of basing the assessment of contributions to the regular budget only on the net budget, thereby excluding the amount of staff assessment or the difference between net and gross salaries. The consequence of this practice is that in UNIDO the Tax Equalization Fund is not funded, since no funds are received which could be credited to the Tax Equalization Fund. Nevertheless, due to the continued applicability of the United Nations Financial Regulations (see GC.2/Dec.25, para. (b)), the official accounts still show the fund as a bookkeeping account.

6. United States nationals and permanent residents have continued to be refunded the amounts paid by them in income taxes levied on their salaries and emoluments from UNIDO. The refunded taxes for the tax years 1986-1989 amount to US$514,091.14, all of which is owed by the United States Government.

II. FINANCIAL AND STAFF REGULATIONS

7. In 1986 and 1987 Member States considered proposals by the Secretariat for new financial and staff regulations for UNIDO. With respect to nearly all other matters than the Tax Equalization Fund, a consensus was reached so that, upon recommendation of the Board, the General Conference at its second session in November 1987 was able to adopt decision GC.2/Dec.25, establishing new financial regulations, and decision GC.2/Dec.29, establishing new staff regulations for UNIDO. Concerning the financial regulations, the General Conference in paragraph (b) of decision GC.2/Dec.25

> "requested the Director-General for the time being to continue to apply, in accordance with Article 26.2 of the Constitution, the provisions of the financial regulations of the United Nations, namely the chapeau and subparagraph (e) of regulation 5.2, concerning those regulations on which no consensus had been reached, namely regulations 5.2 (e) and 5.3."

8. Similarly, concerning the staff regulations, the General Conference in paragraph (c) of decision GC.2/Dec.29

> "requested the Director-General for the time being to continue to apply, in accordance with Article 26.2 of the Constitution, the provisions of the Staff Regulations of the United Nations 3.3 (e), 3.3 (f) and the pertinent provisions of Article XII, concerning those regulations on which no consensus had been reached, namely 6.8 (c), 6.8 (d) and 13.4."

(A text for staff regulation 13.4 was subsequently adopted by the General Conference in its decision GC.3/Dec.27.)

III. PROPOSALS

9. Considering that also in the future there will be only a few staff members that are liable to pay income taxes on their official salaries and emoluments, Member States may consider it desirable to abolish the legal requirement of a Tax Equilization Fund, thereby simplifying the presentation of UNIDO's financial statements and reducing the related unproductive administrative work. By discontinuing the Tax Equalization Fund, Member States also would act consistently with the now firm practice of calculating the assessment for the regular budget only on a net basis, excluding staff assessment. Although in the view of the Director-General it would bring administrative simplification to terminate the Tax Equalization Fund, it would be necessary for legal reasons, when amending decisions GC.2/Dec.25 and GC.2/Dec.29, for the General Conference to adopt (a) a financial regulation requiring any Member State that levies taxes on the official salaries and emoluments of staff members to refund the Organization and (b) a staff regulation authorizing the Director-General to refund staff members the amount of such taxes. Accordingly, the Board may wish to consider the proposals set out below and, if acceptable, recommend them to the General Conference at its fourth session for adoption.

IV. ACTION REQUIRED OF THE BOARD

10. The Board may wish to consider the adoption of the following draft decision:

"The Industrial Development Board:

"(a) Takes note of the report by the Director-General on the Tax Equalization Fund (IDB.8/31);

"(b) Recommends to the General Conference at its fourth session that it

"(i) Decide to delete from the Financial Regulations of UNIDO the text of regulations 5.2 (e), and 5.3, which appear between brackets, and of regulation 10.1 (b)(iii);

"(ii) Decide to adopt instead a new financial regulation 5.3 reading

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5.3. When a staff member, notwithstanding Section 18 (b) of the Convention on the Privileges and Immunities of the United Nations or Section 19 (b) of the Convention on the

Privileges and Immunities of the Specialized Agencies, as applicable, is subject to national income taxation in respect of the salaries or emoluments paid to him or her by the Organization, the Member State levying such taxes shall refund the Organization the amount received during the preceding financial year.';

"(iii) Decide to delete from the Staff Regulations of UNIDO the text of regulation 6.8 (b), last sentence, as well as the text of regulations 6.8 (c) and 6.8 (d) which appears in brackets;

"(iv) Decide to adopt instead a new staff regulation 6.8 (c) reading

'(c) Where a staff member, notwithstanding Section 18 (b) of the Convention on the Privileges and Immunities of the United Nations or Section 19 (b) of the Convention on the Privileges and Immunities of the Specialized Agencies, as applicable, is subject to national income taxation in respect of the salaries or emoluments paid to him or her, the Director-General shall refund the staff member concerned the amount paid during the preceding financial year.';

"(v) Requests the Director-General to implement the above new financial and staff regulations as of 1 January 1992 and to amend the financial and staff rules accordingly."